



## HOMEOWNERSHIP EDUCATION AND COUNSELLING: AN EXAMINATION OF U.S. EXPERIENCE AND ITS RELEVANCE FOR CANADA

### Why This Study is Important

From the mid-1980s to mid-1990s the US homeownership rate stagnated at approximately 64 per cent. In 1995, President Clinton announced a housing sector-wide "National Homeownership Strategy" initiative aimed at raising the rate to 67.5 per cent by 2001. While US research has continually shown that lack of information about how to buy a home was a strong access barrier, middle and high-income households already had extremely high (above 85%) homeownership rates. Increasing the national rate required measures enhancing access to traditionally underserved markets (i.e. minorities, lower-to moderate income households, younger households, dwellers in central cities, immigrants, and rural populations including aboriginals). Such lending however, raised concerns of potentially unacceptable levels of mortgage default risk. Freddie Mac research, however, showed that a notable way of improving borrower-repayment reliability was through the use of homeowner education and counseling (HEC) which emphasized home buyer preparedness.

Over the last five years, there has been renewed interest and activity in the US in expanding the homeownership market using HEC as a means to reach traditionally underserved households while managing mortgage loan default risk. In recognition of HEC's perceived value, the US Housing and Urban Development Department (HUD), non-profit and community development organizations, lenders, mortgage insurers as well as other quasi-government agencies such as Fannie Mae and Freddie Mac have

encouraged, funded, and participated in the delivery and standardization of HEC and in the creation of the American Homeowner Education and Counseling Institute (AHECI). HUD provided further support in the form of reduced (i.e. 30 to 40 per cent) up-front mortgage insurance premiums to first-time homebuyers successfully completing accredited HEC programs.

Since the mid-1990s, HEC has helped raise the US homeownership rate to 67 per cent facilitated by a range of positive environmental factors including:

- sustained US economic growth;
- housing stakeholders' initiatives in response to the National Homeownership Strategy;
- the widespread development and use of affordable housing mortgage loan instruments linked to HEC; and
- downpayment assistance programs run by state and local governments and housing agencies (also linked to HEC).

In such a facilitative environment, HEC sponsors developed successful outreach methods to market homeownership to underserved communities.





## Research Program

The purpose of this research project was to examine the American experience with a view to identifying ways of enhancing affordable, sustainable access to homeownership in Canada. In carrying out the U.S. segment of this research, in addition to conducting a literature review, a survey of HEC providers and participants was conducted together with follow-up interviews. For the Canadian portion of the research, a broad range of housing and community organizations (180 in total) were surveyed and follow-up interviews conducted in order to develop a portrait of existing homeownership access support services in Canada.

The first part of the report provides a comprehensive summary and evaluation of the HEC experience in the US. Following a synopsis of the historical evolution of HEC, the report outlines the characteristics of HEC programs, services and delivery agencies; responses from HEC industry participants surveyed; how HEC is funded as well as recent developments affecting the HEC industry; specifically the establishment of AHECI, the increased focus on standardizing program content and delivery as well as the certification of HEC providers. Next, the report describes the role that HEC has had in addressing credit, affordability, psychological, cultural and linguistic access barriers to homeownership and is followed with a summary of the statistical studies, research and anecdotal evidence assessing the efficacy of HEC both in facilitating access to homeownership as well as in mitigating mortgage loan default risk. This section of the report concludes by summarizing the results of the US HEC industry expert survey in such areas as: the future of HEC and its key factors of success; why industry leaders are so interested in HEC; and outlines respondents' comments on introducing HEC-type initiatives elsewhere.

The second part of the report examines the access support services and delivery structures existing in Canada to help households access homeownership. It examines information and/or access gaps which indicate the need for enhancing homeowner

education and counseling efforts in Canada. The results of a national survey examining the nature, scope and operation of existing homebuyer education and counseling efforts in Canada are then presented followed by an assessment of the differences between what is offered in the US vis-a-vis Canada in addressing access barriers to homeownership. The section of the report concludes by examining whether the gaps in services available in Canada might be filled by introducing HEC-style initiatives that draw on best practices used in the U.S. under the auspices of a housing sector-driven public-private partnership arrangement.

## Findings

### A Review of the U.S. Experience

Homeowner education and counseling got its start in the US as part of the legislation creating HUD in 1968. With significant and ongoing financial support from HUD, and episodic support from lenders and private concerns, the industry expanded from a handful of pilot projects to thousands of providers of a wide range of education and counseling services. Important events in the industry's evolution include the enforcement of the Community Reinvestment Act (CRA) in 1989, which put pressure on lenders to penetrate underserved housing markets; stagnating U.S homeownership rates of the mid 1980s and mid 1990s that spurred interest among the three levels of government in HEC as a vehicle to raise homeownership; and the 1992 Federal Housing Enterprise Financial Safety and Soundness Act that allowed HUD to set affordable housing goals for the Government Sponsored Enterprises (GSEs)--Fannie Mae and Freddie Mac.

Post-purchase foreclosure prevention dominated the industry's early activities. The focus shifted to pre-purchase education and counseling in the early 1990s. Recently, a number of providers have moved to comprehensive "full-cycle" counseling designed to help families both before and after they purchase a home and extending, in some cases, to training for elderly households seeking senior annuity



mortgages. Through its first 25 years, the U.S. industry has been characterized as “fragmented” due to a lack of program content and delivery standards, however, over the last 5 years, various developments, including the creation of the AHECI, have contributed to increased standardization.

## Industry Services

The industry’s four main services are:

- pre-purchase education to help households through the homebuying process;
- pre-purchase counseling to help households overcome financial, credit , linguistic, cultural and psychological barriers to becoming homeowners;
- post-purchase education to instruct homeowners regarding home maintenance, to protect homeowners from predatory lenders and to demystify new mortgage instruments like senior annuity mortgages; and,
- post-purchase counseling to help prevent foreclosure.

Pre-purchase education is general in nature and provided to help households determine whether homeownership is right for them. Some of the largest providers of pre-purchase education provide education over the telephone. Counselling, however, is a more time intensive and expensive exercise that usually includes:

- assessing a family’s ability to buy a home based on income and credit history;
- helping to repair, or establish, credit histories for those with bad or no credit;
- monitoring household income and expenditure;
- advising and assisting clients in finding employment opportunities to increase inadequate incomes; and
- reviewing all aspects of the purchase and the financing of home; and linking lenders with real estate agents, and social service agencies.

Some HEC providers offer other services aimed at facilitating or helping sustain access to homeownership that include:

- assisting homebuyer’s access to favourable mortgage terms through affiliated lenders and underwriting services;
- facilitating access to downpayment and homeownership assistance initiatives offered by state and municipal governments or local housing and community development groups;
- obtaining forbearance from lenders if the client has trouble making mortgage payments; and
- providing post-purchase counseling to assist in money-management, home maintenance, or workout schemes to prevent foreclosure.

HEC agencies are often multifunction organizations that include HEC as one part of a comprehensive low-income homeownership or community development strategy. Other programs in which HEC agencies often engage include:

- affordable housing production;
- rehabilitation and sale of the existing housing stock;
- mortgage underwriting;
- development and/or management of low-income rental property;
- small business development; and
- organizing community programs such as childcare, neighbourhood gardens, neighbourhood watch, sports leagues, etc.

In Tribal areas, HEC agencies have helped address some particularly daunting barriers arising from the lack of a tradition of homeownership and the absence of institutional arrangements to facilitate home purchases. The Navajo Partnership for Housing in Window Rock, Arizona, for example, worked with other groups to develop an instrument which could serve as collateral for a housing loan and overcome barriers associated with the inalienability of tribal lands.



## Agency Characteristics and HEC Trends

The average agency surveyed for this study was a nonprofit organization that had been in operation for more than 18 years and had provided counseling for more than 5 years. The average agency offered 9 hours of classroom instruction and 2.5 hours of one-on-one instruction (not counting tele-HEC). Between 25 and 40 per cent of course graduates became homeowners (71 per cent becoming homeowners within one year and a further 20 per cent within two years). For a majority of agencies surveyed that tracked graduates, delinquency rates for counseling graduates who purchased homes averaged 6-10 per cent while default rates averaged less than 1 per cent (about the average for all mortgages in the US).

HEC delivery agencies reported the following homeownership access barriers addressed facing their clients:

- credit problems (100 per cent);
- lack of savings for downpayment and closing costs (93 per cent);
- lack of knowledge and understanding regarding the home purchase process (79 per cent);
- housing affordability relative to client's income level (77 per cent);
- cultural/linguistic barriers (63 per cent);
- lack of knowledge regarding available housing support (57 per cent);
- lack of availability of decent housing (23 per cent); and
- high construction costs.

Agencies listed the following as among the major strategies they employ to help clients purchase homes:

- budget planning and fiscal discipline (100 per cent);
- demystifying the home purchase process (96 per cent);
- credit repair (79 per cent);

- downpayment and closing cost assistance (57 per cent);
- access to financial assistance, most often in the form of "soft" or "silent" second mortgages with special terms (47 per cent).

More than 25 per cent of recipients received training over the telephone (tele-HEC), however most industry experts hold a dim view of tele-HEC. All but one of the survey respondents felt that HEC could not be delivered effectively over the telephone. Even three of the four representatives of large tele-HEC programs felt that tele-HEC training would not diminish default risk. Further, graduates of tele-HEC training are not eligible for the reduced FHA mortgage insurance premiums offered by HUD.

Other recent trends include: a growth in the number of HEC providers charging clients nominal fees for services; the increasing consolidation of HEC efforts within urban areas; and a movement away from one-on-one counseling to HEC offered in a classroom setting.

In various studies, the costs of delivering HEC range \$100 to \$3200 per client for those that don't require extensive long term counseling support. The lower estimate applies to education courses provided to a large volume of clients (i.e. more than 30 households a month). For households that need long-term counseling to overcome financial or psychological barriers, costs could amount up to \$1000 per client. Governments and lenders contribute almost equally for about two-thirds of HEC delivery costs with user fees and contributions from private sources accounting for the remainder. In some locales, lenders pay a "bounty" to HEC providers for each mortgage closed with one of their counseling agencies which underscores the importance placed in HEC as a marketing and screening device for lenders.



## **American Homeowner Education and Counseling Institute (AHECI)**

AHECI, initiated by Fannie Mae in 1996, received housing sector-wide funding support from lenders, mortgage insurers, construction and realtor associations, mortgage securitizers and HUD to achieve 4 objectives:

- to establish certification standards and evaluation criteria for homeownership educators and counselors;
- to establish a standard core curriculum for homeownership education;
- to perform original research into the contribution of HEC in promoting homeownership and minimizing foreclosure risk; and
- to act as a clearing house for information and resources regarding HEC.

A final lower-priority goal was to make HEC self-financing. AHECI has delivered on its first two goals, but, to date, has not progressed much on the third and fourth goals.

### **Contribution of HEC Programs**

There is some evidence that HEC agencies have achieved the goal of outreach/sorting (based on risk) and expansion of homeownership to underserved populations. Stakeholders who were interviewed agreed that HEC agencies effectively distinguish between the underserved who are: i) already creditworthy but unable to qualify for a conventional mortgage (i.e. an immigrant family with no credit history); ii) able to become creditworthy through education and counseling; and iii) are not good credit risks and should not become owners. HEC agencies benefit lenders by reaching out to these populations, sorting them and getting them “mortgage-ready”.

Credible empirical studies have not yet been undertaken to assess the effectiveness of U.S. programs in reducing the default risk associated with efforts to expand homeownership although several studies (noted in the report) are currently underway. Because of the historically fragmented nature of the

industry and the diversity of clientele and of programs, it has been very difficult up to now to document the impact of HEC. Although the FHA offers 30 to 40 per cent up-front mortgage insurance premium discounts to first-time homebuyers who graduate from HUD-approved HEC training programs, there is not yet statistical evidence showing that these clients pose less risk to the agency. US studies, however, estimate that the total losses that accrue to lenders, mortgage insurers and municipalities average \$73,000 for foreclosures on FHA insured mortgages and \$26,000 on conventional mortgages.

### **The Canadian Scene**

For a variety of reasons, including a different political environment, Canada did not follow the same evolution as the U.S. in promoting and supporting homeownership education in the late 1960s and early 1970s. In the absence of public sector and institutional support, what has emerged is a patchwork of programs and initiatives that are mostly oriented towards information dissemination rather than education and counseling. The main support services for existing and prospective homeowners consist of:

- pre-purchase seminars run by for-profit firms aimed at demystifying the homebuying process;
- workshops offered by nonprofit organizations (including schools) that are occasionally directed at new homebuyers but which are mainly focused on general budgeting and money management issues;
- hardcopy and electronic information on homeownership processes and programs, along with workbooks and decision-making guides for new homeowners, issued by a variety of private and public sector organizations;
- debtor assistance programs operated by governments, for-profit and nonprofit organizations that are not directed specifically at homeowners but may nonetheless serve as vehicle of post-purchase assistance for indebted households;



- a small number of government (pre-purchase, combined in some cases with post-purchase) counseling programs linked to financial assistance programs to facilitate homeownership by low-income households; and,
- pre-purchase and post-purchase education and counseling programs offered in conjunction with a small number of nonprofit housing initiatives targeted at low-income households.

Existing information dissemination measures are unlikely to be reaching some consumers or potential consumers, including minorities who require HEC information and services in languages other than English and French. Moreover, they are unlikely to address the needs of households that require assistance that extends beyond information provision. The latter group includes:

- off-reserve aboriginal households who face special obstacles due to a lack a tradition of homeownership;
- immigrants who require counseling to adapt to cultural differences that affect homebuying and homeownership;
- households with psychological impediments to homeownership;
- households that need to improve their budgeting and financial management skills to prepare for homeownership;
- those with special financial needs and/or risk characteristics who need to build stronger links with mortgage lenders; and
- homeowners that would benefit from advice and support intended to guide them towards more sustainable homeownership practices.

Given the US experience, Canadian programs appear unlikely to be meeting the needs of households that could benefit from post-purchase counseling. Existing Canadian programs serve only some participants in government or nonprofit-sponsored assisted housing programs and homeowners who have already encountered financial difficulties and have been led to seek debt management assistance. For most

homeowners, there is no ready access to the advice and support that may be required to help them sustain homeownership.

## Conclusions

Canada does not have an identifiable HEC industry, but it does have a wide range of organizations that provide information and support services to prospective and existing homeowners. Information gaps that exist cannot be attributed to the lack of published and electronic resources available for new homeowners. Nor do they reflect the inadequacy of information provided through the new homeowner seminars sponsored by for-profit firms. While there appears to be considerable scope to expand their coverage and improve their effectiveness, homeowner seminars largely address the needs of households that simply require very basic information on the homebuying process and on the calculations that will help them determine what they can afford. The problems are rather that:

- (i) existing mechanisms of information dissemination are not reaching some consumers, or potential consumers; and
- (ii) some households require assistance that extends beyond basic information provision.

The counseling services currently available in connection with the assisted housing programs operated by governments and nonprofit organizations are reaching only a small segment of those households in need of more extensive assistance.

Many homeownership support requirements that are not being met in Canada are being addressed in the US. For housing stakeholders in Canada interested in enhancing access to homeownership by developing a US HEC-style initiative consideration should be given to adopting an appropriate strategy - one that is in keeping with the potential significance of HEC and also the lack of solid evidence documenting the ability of HEC to reduce default risks.



## **Characteristics of a Well-Designed HEC Program**

U.S. survey respondents felt that the U.S. experience suggests that successful HEC programs are likely to include:

- (1) A approach that reflects a full understanding of local housing conditions and local populations.

Because the condition of housing, population demographics, and labor markets vary dramatically from place to place, it is important that the approach adopted by a HEC agency is consistent with local needs. Without decent affordable housing available locally, educating potential home buyers will not generate very positive results. If the local population has a high proportion of immigrants, instruction given in English might not be appropriate. Legal documents, special lending products, and public support also vary locally. An effective HEC program must be well integrated in its locality.

- (2) An Effective Outreach Mechanism

All successful HEC programs have found effective means of reaching its clientele. This involves the use of both formal (radio, television, or newspapers) and informal channels (linking with employers, churches, or community groups; posting flyers).

- (3) A Carefully Planned Classroom Education Component

Most observers agree that HEC cannot be effectively delivered over the telephone. Classroom instruction is required based on an approved core curriculum and incorporating modules that address local issues and concerns. The course should be targeted at households that have not yet begun the home search process. It should be offered by certified instructors and participants should be tested before graduation.

- (4) A Complementary Component of One-on-One Counseling

This is often necessary where clients need help improving their budgeting and money management skills and repairing their credit history. HEC counselors should be certified and required to adhere to an industry code of ethics.

- (5) The Support of Umbrella Agencies

In the U.S. umbrella agencies fulfill an important support function. They develop the curriculum, produce and distribute educational materials, train instructors and undertake research and program assessments. Umbrella organizations help to ensure HEC providers satisfy minimum standards in terms of course content and delivery, and help providers realize the economies from a joint approach to certain common functions.

- (6) Links to Organizations offering related Services

Well-developed links to other organizations serve three functions. First, they help HEC providers reach households who could benefit from homeownership education and counseling. Second, through such links, HEC providers will be well positioned to help households that require assistance beyond homeownership education and counseling - such as language or job training. Third, HEC providers can help households to seek other homeownership support offered through public agencies, employers, or lenders.



## A Proposed Approach

The study concludes that there appears to be sufficient positive evidence from case studies, the views of industry participants and the continued willingness of U.S. stakeholders to contribute to U.S. programs to consider an exploratory entry into the provision of HEC in Canada, most likely through a partnership amongst housing sector stakeholders with the most to gain. Preparatory work to lay the groundwork for the possible development of a HEC industry could include the development of HEC demonstration projects. A steering committee representing the main stakeholders could assess the experimental HEC projects in Canada and monitor the results of a number of large-scale research projects that are underway to evaluate the effectiveness of U.S. HEC initiatives. Stakeholders could work together to create programs that draw on the best features of the U.S. experience to address gaps in the services available to assist potential and existing Canadian homeowners.

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**Research Report:** *Homeownership Education and Counselling: An Examination of U.S. Experience and its Relevance for Canada*

**Research Consultants:** Ron Hirshhorn, Hirshhorn Consulting, Inc., Nepean, Ontario; George McCarthy, University of North Carolina, Chapel Hill, U.S.A.

A full report on this project is available from the Canadian Housing Information Centre at the address below.

### Housing Research at CMHC

Under Part IX of the *National Housing Act*, the Government of Canada provides funds to CMHC to conduct research into the social, economic and technical aspects of housing and related fields, and to undertake the publishing and distribution of the results of this research.

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For a complete list of **Research Highlights**, or for more information on CMHC housing research and information, please contact:

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